International Journal of Sciences: Basic and Applied Research (IJSBAR)

IJSBAR International Journal of Sciences: Basic and Applied Research

ISSN 2307-4531
(Print & Online)

http://gssrr.org/index.php?journal=JournalOfBasicAndApplied

The Role of Financial Audits on Effective Corporate Governance in Companies: A Case Study of Coastal Bottlers Limited

Johnson Amani Changawa[a*], Fridah Simba Theuri[b]

[a]*Department of Economics and Commerce, School of Human Resource Development (SHRD), Jomo Kenyatta University of Agriculture and Technology,P. O. Box 81310, Mombasa, 80100, Kenya*

[b]*Graduate Student,Department of Economics and Commerce, School of Human Resource Development (SHRD), Jomo Kenyatta University of Agriculture and Technology, P. O. Box 81310, Mombasa, 80100, Kenya*

[a]*Email: jbomu@yahoo.com*

[b]*Email: Fridahtheuri@gmail.com*

Abstract

The financial audit remains an important aspect of corporate governance that makes management accountable to shareholders for its stewardship of a company. The audit serves as a signaling mechanism to shareholders of a company that information provided by the company's directors can be relied upon. However despite all positive aspects attributable to the roles played by financial auditors, recent experience indicate that companies have not managed to reach their optimal operational efficiency level either because of failure to engage effective independent auditors or failure to accord the auditors their rights as auditors in their engagement execution. The objectivesof the study was to examine the role of financial audits, internal control systems, financial statements, analytical procedures and the role of auditor's reports on effective corporate governance in companies.

The study was conducted in Coastal Bottlers Limited in Kilifi County, Kenya. Data was collected from seventy eight respondents using stratified random sampling techniques. Questionnaires were administered and responses analysed using both qualitative and quantitative techniques and presented in tables and interpreted using pie charts and graphs.

Results revealed that, internal control systems such as internal checks and balances reduce costs due to theft and pilferages; provide assurance on the reliability of financial information generated through the company's financial statements. Financial Statements provide important managerial information for planning, monitoring performance and decision making. Analytical procedures such as ratio analysis and ageing analysis provide the management with information to evaluate data and isolate the problematic areas. Financial auditor's reports enable management to know whether they are compliant in all respect to laws and standards; provide confidence to the stakeholders about the efficiency and effectiveness of the management's operational and control systems through encouraging transparency and accountability.

Keywords:Financial Audits; Corporate Governance; Internal Control Systems; Analytical Procedures; Financial Statements.

1. Introduction

1.1 Background Information

One of the most far reaching consequences of the Industrial Revolution was the introduction of the limited liability company. The first such was registered at Companies House in 1856 and this, in essence, signaled the final, formal, split between ownership and control. Prior to the UK Companies Act (1856) many ventures had been financed through the medium of the joint stock company – such as the Hudson's Bay company formed in 1670 and the East India Company formed in 1600 – whereby a group of investors financed a venture using a joint stock company managed by an elected board of directors. However, to do this required a Royal Charter or Act of Parliament. The great advantage of using these companies was, of course, limited liability, the great disadvantage being the cost and the ponderous process of setting them up. Only the wealthy could afford to do this.

The right of anyone to set up a company with limited liability, which was introduced in 1856, signified the creation of the modern company. The law and regulations which have grown up around it to regulate its actions of its members and managers stem from these nineteenth century origins. Whilst the modern company came into being in 1856, the audit profession came somewhat later, it was not until the UK Companies Act (1900) that an obligation to produce annual accounts was placed on the directors of companies. It is from 1900 that financial statements became the basic mechanism by which the activities of company managers were monitored, and to some extent, this is still true today. Once the directors were required by law to prepare annual financial statements shareholders then had access to financial information about the company they owned. However, this access was limited and the shareholders may come to believe that they are not getting all the information, or the right information to enable them to make investment decisions. Thus the role of the auditor as agent for the shareholders becomes crucial and the costs of the audit are as nothing with the comfort and reassurance the audit affords the shareholders. The independent audit is a crucial part of this process to ensure that the financial statements faithfully represent the activities of the managers during the financial period.

[23] defined financial audit as consisting of evaluation of a subject matter with a view to express an opinion on whether the subject matter is fairly presented. The Auditing Practices Board (APB), which is the body responsible for issuing auditing standards and guidance states: ‘The objectives of an audit of financial statements are: to enable the auditor to express an opinion whether the financial statements are prepared in all material respect in accordance with an applicable financial reporting framework.’; to produce a report by the auditors of their opinion of the truth and fairness of financial statements so that any person reading and using them can have belief in them; to advise management of any defects or problems with their accounting systems and to suggest ways of improving it; to prevent errors and fraud by the deterrent and moral effect of the audit.

The Auditing Practices Board (APB), which is the body responsible for issuing auditing standards and guidance states the objectives of audit of financial statements as to enable the auditor to express an opinion whether the financial statements are prepared in all material respect in accordance with an applicable financial reporting framework; to produce a report by the auditors of their opinion of the truth and fairness of financial statements so that any person reading and using them can have belief in them; to advise management of any defects or problems with their accounting systems and to suggest ways of improving it; to prevent errors and fraud by the deterrent and moral effect of the audit.

The way in which companies are run and controlled has been a matter of concern to the government, the Stock Exchange, the investing community, lawyers and auditors for many years. The matter is known as corporate governance and includes issues of accountability as well as management and organisation. The genesis of corporate governance can be dated to 1992 with the publication of the Cadbury Report. During the 1980s there had been a prolonged period of economic growth which, by the early 1990s, was beginning to go into reverse. Companies which had previously shown signs of spectacular success were shown to be built on sand, or at least very high borrowings, and the successive collapses, in the UK, of Coloroll, Polly Peck and Maxwell Communications Corporation, which took with it the pension fund of Mirror Group Newspapers, prompted public concern. This was exacerbated by the £8bn collapse of the Bank of Credit and Commerce International, which was subsequently revealed to be a hotbed of fraud and illicit dealings, and the debacle of Delorean which took with it about £80m of public money. Thousands of individuals had lost their savings and public concern was mounting. The City reacted quickly and commissioned Sir Peter Cadbury to come up with some good practice proposals which would reinforce the responsibilities of executive directors; strengthen the role of the non-executive director; make the case for audit committees of the board; restate the principal responsibilities of auditors; and reinforce the links between shareholders, boards and auditors.

[6]drew up guidelines that were published in July 2003 as part of its Combined Code on Corporate Governance. The council required the board to present a balanced and understandable assessment of the company’s position and prospects. The board’s responsibility to present a balanced and understandable assessment extends to interim and other price-sensitive public reports and reports to regulators as well as to information required to be presented by statutory requirements. The directors should explain in the annual report their responsibility for preparing the accounts and there should be a statement by the auditors about their reporting responsibilities. The directors should

report that the business is a going concern, with supporting assumptions or qualifications as necessary. It is now part of the listing agreement of the Stock Exchange and listed companies to conform to the code.

[17] definedgoing concern as a business that is currently operating, and which shows that it intends to keep operating. That is, the business is not being run as if it were going to close soon. The concept of going concern includes a current active base of regular or occasional customers; a mailing list or customer record file would be a good way to estimate this customer base; employees who know the business and who have developed strong business relationships with customers and vendors; equipment, supplies, furniture and fixtures that are in good condition and are still being depreciated; verifiable profits over several years, as evidenced by income tax records; positive cash flow (an ability to pay business expenses), and an ability to pay off the long-term debts of the business on a regular basis. A business which is a going concern has a high value to investors, as opposed to the value of a business that is failing or closing.

Statement on Auditing Standard (SAS) 600 (1993) requires Auditors to read and report on the corporate governance for all listed companies. The whole question of Corporate Governance was dominated by the financial scandals of the early part of the twenty first century in the USA surrounding, in particular, Enron and the lesser, but no less shocking, scandals involving WorldCom, Tyco International, Global Crossing and many others. All of the major accounting firms had clients who were caught up in these scandals, the apotheosis being the destruction of the worldwide accounting firm of Arthur Andersen.

[22]were the co-sponsors of the Sarbanes Oxley Act published in the USA and designed to enforce corporate accountability through new requirements, backed by stiff penalties. Sect.404 of the Act: Assessment of internal control; required company executives to certify and demonstrate that they have established and are maintaining an adequate internal control structure and procedures for financial reporting. This required them to ensure that all the financial reporting systems, including the ancillary systems such as procurement and HR, are functioning in such a way as to prevent material misstatements appearing in the financial accounts – and it is a personal liability. Under sect. 906: Criminal Penalties for CEO/CFO financial statement certification; the Act required chief executives and chief financial officers to personally certify the accuracy of financial statement with a maximum penalty of 20 years in jail and a £5m fine for false statement.

Like any other corporate reports, the corporate governance report's basic purpose is to inform and disclose relevant information to shareholders and other stakeholders of the status of its corporate governance. Specifically, the corporate governance report is expected to inform shareholders and all other stakeholders that its board of directors are conscious and indeed have tried to comply with good corporate governance principles including that it is well composed and duly constituted board, that it is responsible and in control of the company, that those who deal with the company should have the confidence that the company can be relied upon as responsible corporate citizen and it has not been reckless and that the board has duly executed its mandate during the period. [15].

As the results in [15] indicates that there has been a global trend to require reporting and disclosure of matters of interest to corporate governance in many regimes: USA, EU, UK, SEA, Kenya, South Africa, e.t.c. Today codes or guidelines specifically require that a corporate governance report be published. Indeed in some regimes, India as an example, is now required under their company law. In others, e.g. South Africa 2008 Companies Act requires certain aspects of corporate governance to be reported.

In June 2011, the Commissioner of Insurance issued “Corporate Governance Guidelines pursuant to Section 3A of the Insurance Act with the aim of enhancing good corporate governance practices by insurers to protect the interest of shareholders, policyholders and stakeholders”. It is now a requirement that all directors of insurance companies be trained and confirm through reporting that they have indeed undertaken such training among other matters of interest to corporate governance [15].

1.2 Statement of the problem

Supervision and monitoring of management performance (the enterprise aspect) and ensuring accountability of management to shareholders and other stakeholders (the accountability aspect) are some of the aspects which are considered to be fundamental to corporate governance. Recent corporate collapses have established the need for emphasis on substance of the transaction rather than legal form, transparency and the management of risk. An effective internal control system not only helps to minimise financial, operational and compliance risks, but also enhance the quality of financial reporting. As well as playing a fundamental role in transmitting financial results to the general public.

A company operating under statutory standards such as a bank, a hedge fund or an insurance company could include additional information in the financial statements or management disclosures to inform investors about regulatory developments. A company could also voluntarily reveal important developments in its activities by including a ‘Management Discussions and Analysis’ section in regulatory filings. In this section, the firm's managers could inform investors about upcoming reorganization initiatives such as mergers or acquisitions, industry trends, regulatory changes and top management long-term strategies.

This tension is the consequence of information asymmetries produced by the separation of ownership and management. [7] Noted that firms had incentives to offer voluntary disclosures in order to avoid the discounting of firm value resulting from information asymmetries. In addition to the benefits and costs of disclosure, information uncertainty resulting from the separation of ownership from management can also drive the extent of disclosure. [21] Suggested that limited disclosure may be optimal when outside parties are unsure whether or not the firm has private information. In order to alleviate the effects of this information asymmetry firms may employ high quality auditors to provide credibility to their limited disclosures. [2] Studied the voluntary disclosure of reserves by oil and gas companies. They found a weak positive association between the presence of a high quality auditor and disclosure.

Questions have been raised concerning the effectiveness of analytical procedures as a means of accumulating audit evidence. [18] Explained that analytical procedures are useful for the auditor with respect to detecting overstatements of revenue, fictitious sales and receivables, fictitious and overvalued inventory, understated bad debts and allowances for doubtful accounts, unrecorded purchase liabilities, under accrual of expenses, and inappropriate expense capitalization. Analytical procedures, used effectively in those situations, would have revealed unusual relationships and significant changes in relationships. By following up the unusual relationships and the changes in relationships with other audit procedures, the auditor could have detected large errors in the financial statements.

[5] Defined corporate governance as the structures and processes for the direction and control of companies. Corporate governance concerns the relationships among the management, Board of Directors, controlling shareholders, minority shareholders and other stakeholders. Good corporate governance contributes to sustainable economic development by enhancing the performance of companies and increasing their access to outside capital.

Corporate governance aims to resolve problems which arise from the principal-agent relationship, whereby owners have an interest in maximizing the value of their shares – whereas managers tend to be more interested in the private consumption of firm resources and the growth of the firm. It addresses such problems through the contract drafting process and others measures which are developed. One measure which could contribute to corporate governance efforts in addressing the agency problem is the external auditor’s involvement. The financial auditor would facilitate a situation whereby managers are encouraged or compelled to be held more accountable. Through an appropriate application of accounting policies, the external auditor could help facilitate a position whereby creative accounting practices and hyper inflation/inflation of figures are discouraged. Penalties could be imposed on managers and directors who intentionally or recklessly inflate or manipulate accounting figures and financial statements. The likelihood of a qualified audit opinion (as regards the auditor’s findings on the financial statements) is considered to be effective as a deterrent to such managers – particularly where an individual manager or few managers are responsible for fraudulent related acts.

The financial audit remains an important aspect of corporate governance that makes management accountable to shareholders for its stewardship of a company. The audit serves as a signaling mechanism to shareholders of a company that information provided by the company’s directors can be relied upon.

Auditing standards have a role to play in ensuring that factors such as objectivity, integrity and independence, factors which are essentially in the financial auditor’s performance of his responsibilities, are respected. However attention has been drawn to the importance of other issues such as enforcement and disclosure standards: The quality of reported financial information, however, is influenced not simply by the quality of accounting standards, but also by other institutional factors [corporate governance, the legal system, and the existence and enforcement of laws governing investor protection and disclosure standards] that affect the demand for and the supply of financial information. The engagement of external auditor to undertake non routine tasks include the fact that non routine tasks are not only non repetitive by nature, they also require specialized knowledge which internal auditors may not be able to acquire in house. Further, the use of external auditors in performing non routine tasks may be more efficient.

However despite all positive aspects attributable to the roles played by financial auditors, recent experience indicate that Coastal Bottlers Limited still has not managed to reach its optimal operational efficiency level either because of failure to engage effective independent auditors or failure to accord the auditors their rights as auditors in their engagement execution.

This document is meant to establish some of the roles played by financial audits which if well performed may result into an effective corporate governance in companies and avoid corporate failures.

1.3 Objective of the Study

1.3.1 General Objective

To examine the role of financial audits on effective corporate governance in companies

1.3.2 Specific Objectives

a. To establish how internal control systems contribute to effective corporate governance in companies.
b. To establish how financial statements contribute to effective corporate governance in companies.
c. To establish how analytical procedures contribute to effective corporate governance in companies.
d. To establish how auditor's reports contribute to effective corporate governance in companies.

1.4 Research Questions

a. How do internal control systems contribute to effective corporate governance in companies?
b. How do financial statements contribute to effective corporate governance in companies?
c. How do analytical procedures contribute to effective corporate governance in companies?
d. How do auditor's reports contribute to effective corporate governance in companies?

1.5 Justification of the Study

Since the 1997 financial crisis, governments and international organizations have made efforts to reform corporate governance. Notwithstanding new laws and regulations, theory suggests that entrepreneurs requiring external capital would have incentives to mitigate their agency problems by introducing monitoring and/or bonding mechanisms. They would voluntarily tie their hands when the expected benefit of the external financing exceeds the expected gain from expropriating outside investors. In particular, the entrepreneurs may voluntarily employ reputation intermediaries to assure outside investors about their credibility.

In this paper, we investigated whether independent external auditors can serve a corporate governance role by testifying the quality of accounting information. The appointment of quality auditors serves as an assurance to the investors that the companies' financial disclosures would be accurate and truthful. The assurance is credible because the auditors, with their reputation at stake, will closely scrutinize their clients' books and truthfully disclose their findings. However, whether or not auditors in practice fulfill the quality assurance role and hence mitigate the agency problem has been a subject of debate.

Auditors potentially have a stronger governance role because legal systems and the other conventional corporate control systems are weaker in protecting investors. This is supported by the fact that with the presence of Big Five accounting firms and other international firms, the market for external auditors according to William Davidson Institute Working Paper 400 (as cited in [16]) is much more vibrant than the market for takeovers or independent directors. On the other hand, the relationship-based transactions and the under-development of the domestic accounting profession may have considerably reduced the demand and supply of quality audits. Evidence in a United Nations report calls into question if external auditors actually serve as monitors. The report queries why many external auditors had issued clean auditing opinions to clients that later went bankrupt within a few months after the completion of the audits.

1.6 Limitation of the study

It was difficult in making interview appointment with the senior members of staff due to their busy schedules. However, the researcher addressed most of the respondents during the lunch break and after office hours to avoid interference with their routine schedules.

It was difficult to get adequate reading materials for better understanding of the topic. There were insufficient materials on the research topic in the university library. The researcher however got some relevant materials from the internet and other universities' libraries.

Getting access to some information and reaching targeted interviewee was hard. Some of the interviewees were not fully conversant with the study. The researcher however met the interviewees during non-office hours to clarify on any questionnaires' questions not clear to the respondents.

To find the appropriate literature review for this study was hard. Very few researchers had researched on the research topic. This made it difficult for the researcher to conduct sufficient literature review on the study topic. The researcher however maximized on all the available materials and internet documents to get the necessary literature.

2. Materials and Methods

2.1 Introduction

The methods used for this particular research included the research design, the population of the study and its sample size, the various types of data collection instruments used, the sampling techniques, the various data types and their sources and finally the data presentation and analysis techniques.

2.2 Research Design

[1]defineda research design as the plan and structure of investigation so conceived on to obtain answer to research questions. In this case, the researcher adopted a descriptive research design as involved gathering data that described events, organized, tabulated, depicted and described the data collection and also used visual aids such as graphs and charts to aid the reader in understanding the data distribution [20].

The researcher used descriptive research design to enable him collect the relevant data from the respondents using questionnaires, qualitatively and quantitatively analyse the data presented in tables. The data was then interpreted by the use of pie charts and graphs.

2.3 Target Population Study

Coastal Bottlers Limited has 290 employees with 150 of these being on the supervisory and managerial capacities. The target population for this study was the 150 employees. The target population consisted of head of departments, head of sections, and supervisors in the company.

Table 2.1 Target Population

Department	Target Population	%
Finance	9	3.1
Stores	8	2.7
Production	48	16.6
Quality Assurance	25	8.6
Sales and Marketing	60	20.7
Total	150	51.7

2.4 Sample Size

[3]defined sampling as the selection of some part of an aggregate or totality on the basis of which a judgement or inference about the aggregate or totality is made. The sample size was based on 60% of the target population which the researchers subjectively considered to be reasonable and representative of the target population.

Table 2.2 Target Population and Sample Size

Department	Target Population	Sample size	%
Finance	9	5	5.6
Stores	8	5	5.6
Production	48	29	32.2
Quality Assurance	25	15	16.6
Sales and Marketing	60	36	40.0
Total	150	90	100

2.5 Sampling Frame

The sampling procedure used was random selection with 60% of the target population sampled from the various departments. Sub groups within the departments were used as stratified samples from which random selection was done. These subgroups were section heads and supervisors. Larger numbers were selected from larger subgroups to get proportional sampling.

2.6 Sample and Sampling Techniques

The study employed stratified random sampling techniques to develop the sample components. [3]discussed that if a population from which a sample is to be drawn does not constitute a homogeneous group, stratified sampling technique is generally applied in order to obtain a representative sample. The target population in Coastal Bottlers Limited was divided into several sub populations that are individually more homogeneous than the total target population. It grouped the target population into departments, sections and supervisory levels.

2.7 Data Collection Instruments

Research Instruments are measurement tools which will be designed to obtain data on the research topic. Questionnaires were administered on the employees of Coastal Bottlers Limited within the various departments. This was necessary so as to find out their views at different levels. [3]defined a questionnaire as consisting of a number of questions printed or typed in a definite order on a form or set of forms. The researcher preferred to use this instrument as is free from bias from the interviewer, respondents have adequate time to give well thought out answers and even large samples can be reached.

2.8 Data Collection procedure

The researcher introduced the objective of the research to the candidates included in the sample. Questionnaires were then circulated to the various employees who were then asked to answer the questions on their own and return the duly completed questionnaires to the researcher within a week time.

2.9 Data Processing and Analysis

According to [3], the data collected has to be processed and analysed in accordance with the outline laid down for the purpose at the time of developing the research plan. The data collected from the respondents was analysed using both qualitative and quantitative techniques and presented in tables then interpreted by the use of pie charts and graphs.

3. Results and Discussions

3.1 Introduction

The data collected from the various respondents was presented in tables before it was analysed. The analysis was done with the help of graphs and pie chart for better interpretation and understanding.

3.2 Response Rate

The target population sample size who responded was analyzed as below:-

Table 3.1: Response Rate

Department	Numberof questionnaires distributed	Number of questionnaires received back	Percentage (%)
Finance	5	5	5.6
Stores	5	5	5.6
Production	29	26	28.9
Quality Assurance	15	13	14.4
Sales and Marketing	36	29	32.2
Total	90	78	86.7

Source: Author’s own research – Coastal Bottlers Limited

Table 3.1 and Figure 3.1 above indicated that 5.6% of the respondents were from the finance department, 5.6% of the respondents were from the stores department, 28.9% of the respondents were from the production department, 14.4% of the respondents were from the quality assurance department and 32.2% of the respondents were from the sales and marketing department.

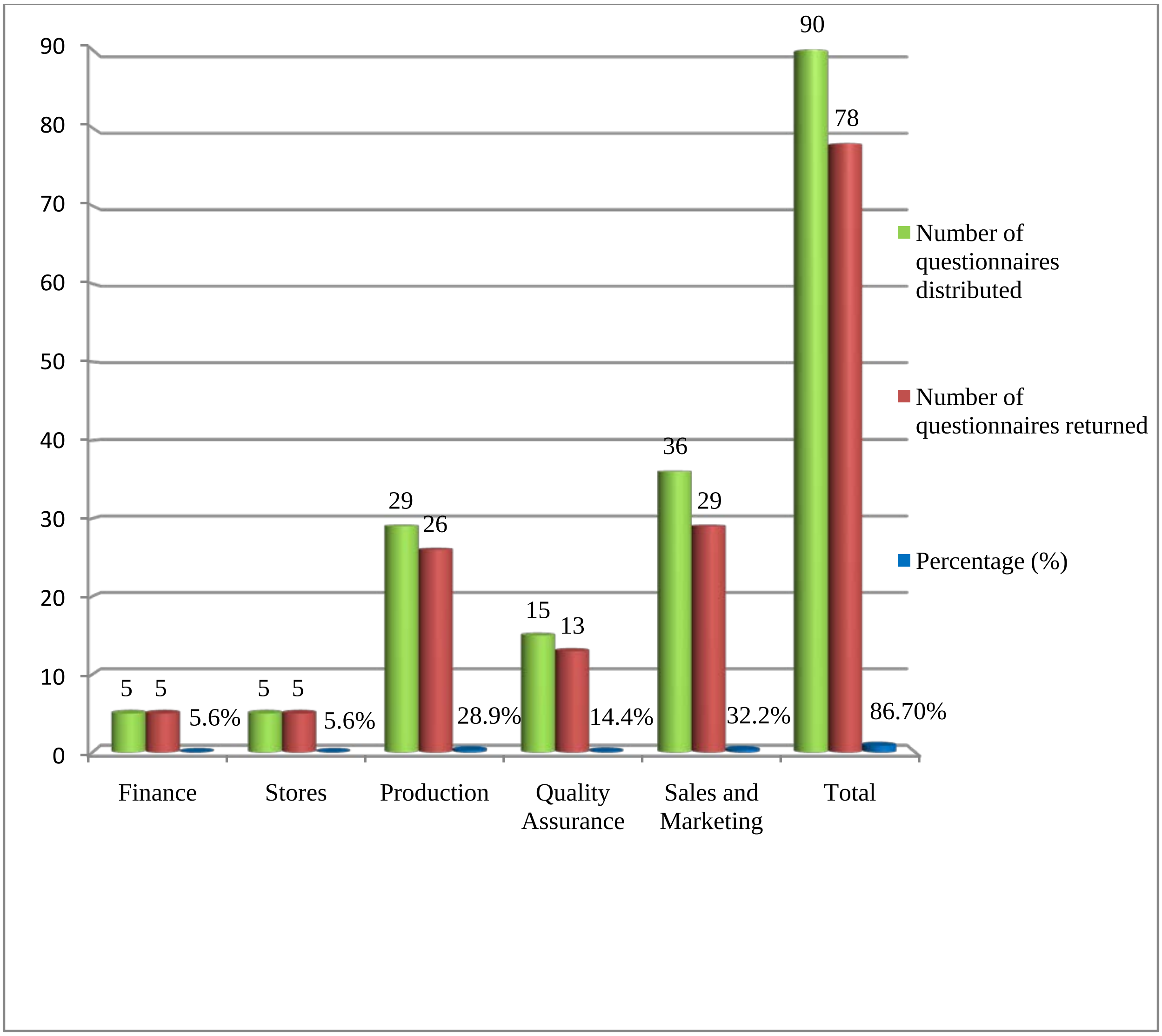

Figure 3.1 Response Rate

It was clear that majority of the respondents were from two departments – production and sales and marketing departments with 28.9% and 32.2% respectively. These two departments account for an important part of the researcher's study since they deal with the engine of the company business of producing and selling of bottled soft drinks. Quality assurance department directly and indirectly determine the extent of activities in the production department by approving the standard of input materials to be used in the production process and thus the quality standard of the output products to be available to the sales department for sale. Stores and finance department had the best response as all sampled employees returned back their fully completed questionnaires. The stores department plays a supplier position to the production department for all the production materials thus directly affects the performance of the company. It was thus clear that majority of the sampled employees responded well and represented fairly the targeted population.

From the total 90 questionnaires distributed, 78 questionnaires which reflected 86.7% of the questionnaires distributed indicated a good response rate and a good representation of the sample size of the target population.

3.3 Gender of Respondents

The gender of the sample size which responded was composed as below:

Table 3.2: Gender of Respondents

Gender of Respondents	Frequency	Percentage (%)
Male	51	65.4
Female	27	34.6
Total	78	100

Source: Author's own research – Coastal Bottlers Limited

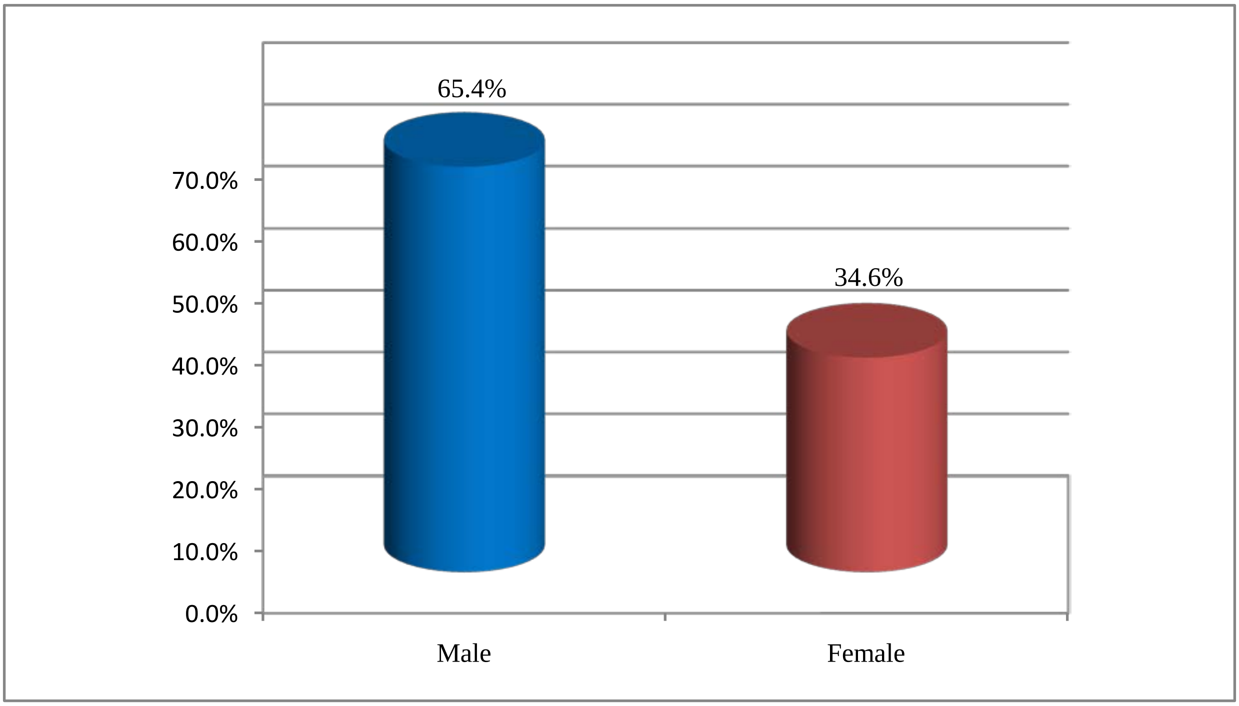

Figure 3.2: Gender of Respondents

Table 3.2 and Figure 3.2 above showed that there were significantly high number of male respondents as compared to the female respondents which is reflected by 65.4% of the respondents being male and 34.6% of the respondents being female. This was attributed to the fact that significant portion of the departments are run by technical staff majority of whom are male.

3.4 Working Experience of Respondents

The respondents' working experience with the company is analysed as below:

Table 3.3: Working Experience of Respondents

Working Experience of Respondents	Frequency	Percentage (%)
Less than 1 year	5	6.4
1-5 years	70	89.7
6-10 years	3	3.9
Total	78	100

Source: Author's own research – Coastal Bottlers Limited

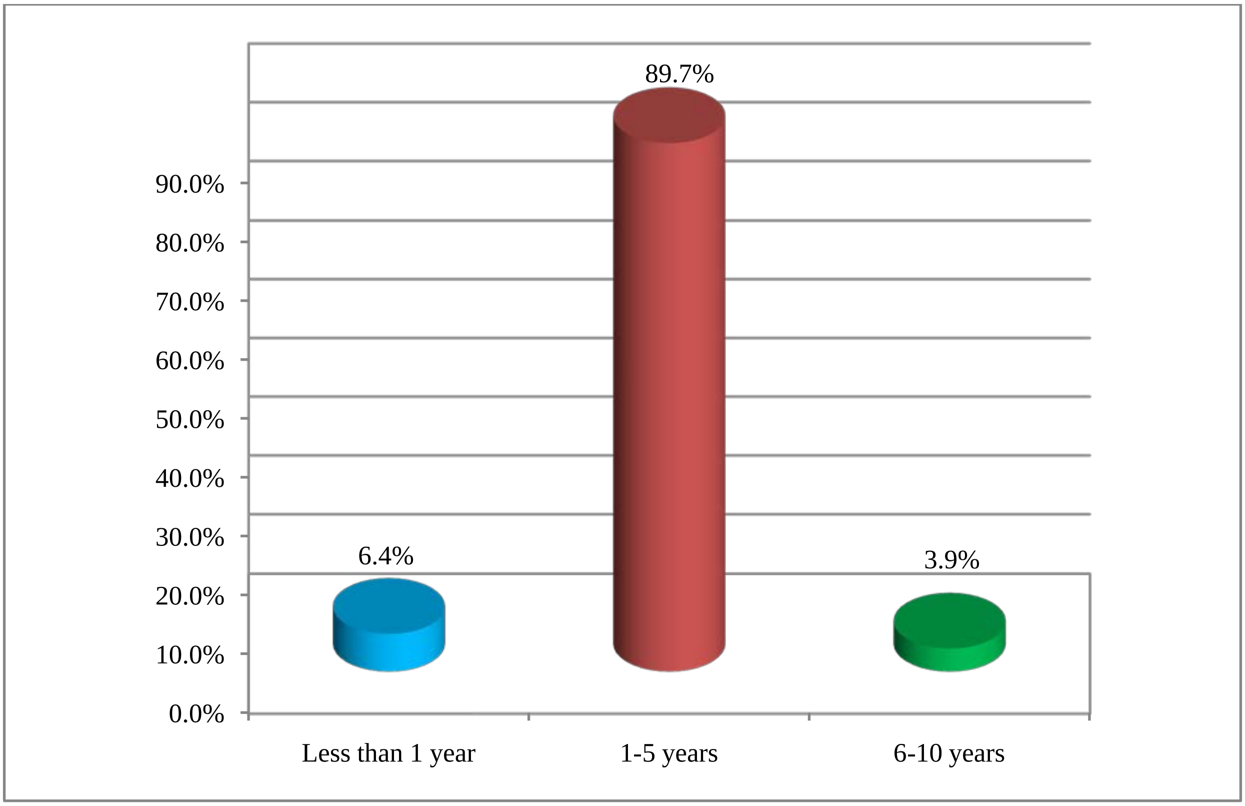

Figure 3.3: Working Experience of Respondents

Table 3.3 and Figure 3.3 above showed that, 6.4% of the respondents had worked at Coastal Bottlers Limited for less than one year, 89.7% of the respondents had worked at Coastal Bottlers Limited between 1 and 5 years, 3.9% of the respondents had worked at Coastal Bottlers Limited between 6 to 10 years

Majority of the respondents had worked more than one year at Coastal Bottlers Limited. This is a considerable good experience for the respondents to shed light on the company's governance styles adopted over a number of years since there had been changes in governance within the last 10 years. None of the employees had worked for more than 10 years due to an overhaul on the management and supervisory employees which took place in 2007 when the company shifted to the current operational area from the Mombasa Island. In 2009, there was a change in the financial auditors and during the last one year, there had also been a change in the general management position.

The pattern of changes both in management and financial auditors gave the respondents with at least one year experience the best position to provide responses on the research topic on the role of financial audits on effective corporate governance.

3.5 Forms of Internal Control Systems (ICSs) in the company

The various internal control systems in existence in the company are analysed below:

Table 3.4: Forms of Internal Control Systems (ICSs)

Forms of Internal Control Systems (ICSs)	Frequently	Percentage (%)
Retail Data Collection	27	34.6
Segregation of duties	51	65.4
Internal checks and balances	60	76.9
Use of CCTVs on physical assets	31	39.7
Cash on order	29	37.2
Authorisation and approval of transactions	40	51.3
Daily physical stock taking and reconciliations	52	66.7

Source: Author's own research – Coastal Bottlers Limited

From Table 3.4 and Figure 3.4 above, it was clear that, 34.6% of the respondents described Retail Data Collection as a form of internal control system in place in the company; 65.4% described Segregation of duties; 76.9% described Internal Checks and balances; 39.7% described use of CCTVs on physical assets; 37.2% described Cash on order; 51.3% described Authorisation and approval of transactions while 66.7% of the respondents described Daily physical stock taking and reconciliations as internal control system as in place in the company.

From the above analysis, it is clear that majority of the respondents described segregation of duties, internal checks and balances and Authorization and approval of transactions and Daily physical stock taking and reconciliations as internal control systems which a company can use to enhance and strengthen its reliability of financial information reflected in its financial statements.

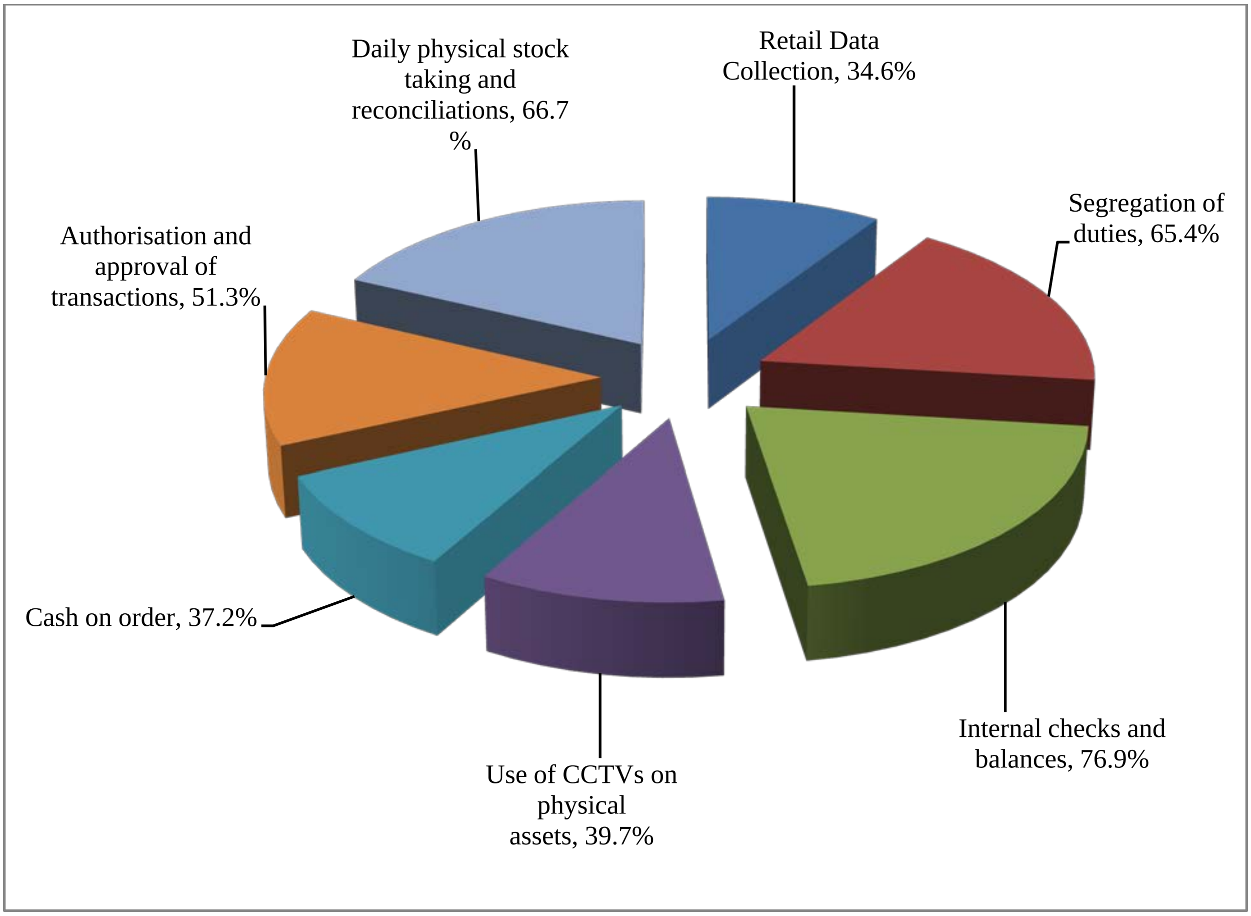

Figure 3.4: Forms of Internal Control Systems (ICSs)

3.6 Whether Internal Control Systems assist in improving the effectiveness of Corporate Governance

The respondents understanding of whether Internal Control Systems assist in improving the effectiveness of corporate governance was presented and analysed as below:

Table 3.5: Whether Internal Control System can assist in improving the effectiveness of Corporate Governance

Whether Internal Control System can assist in improving the effectiveness of corporate governance	Frequency	Percentage (%)
Agree	71	91.0
No idea	7	9.0
Total	78	100

Source: Author's own research – Coastal Bottlers Limited

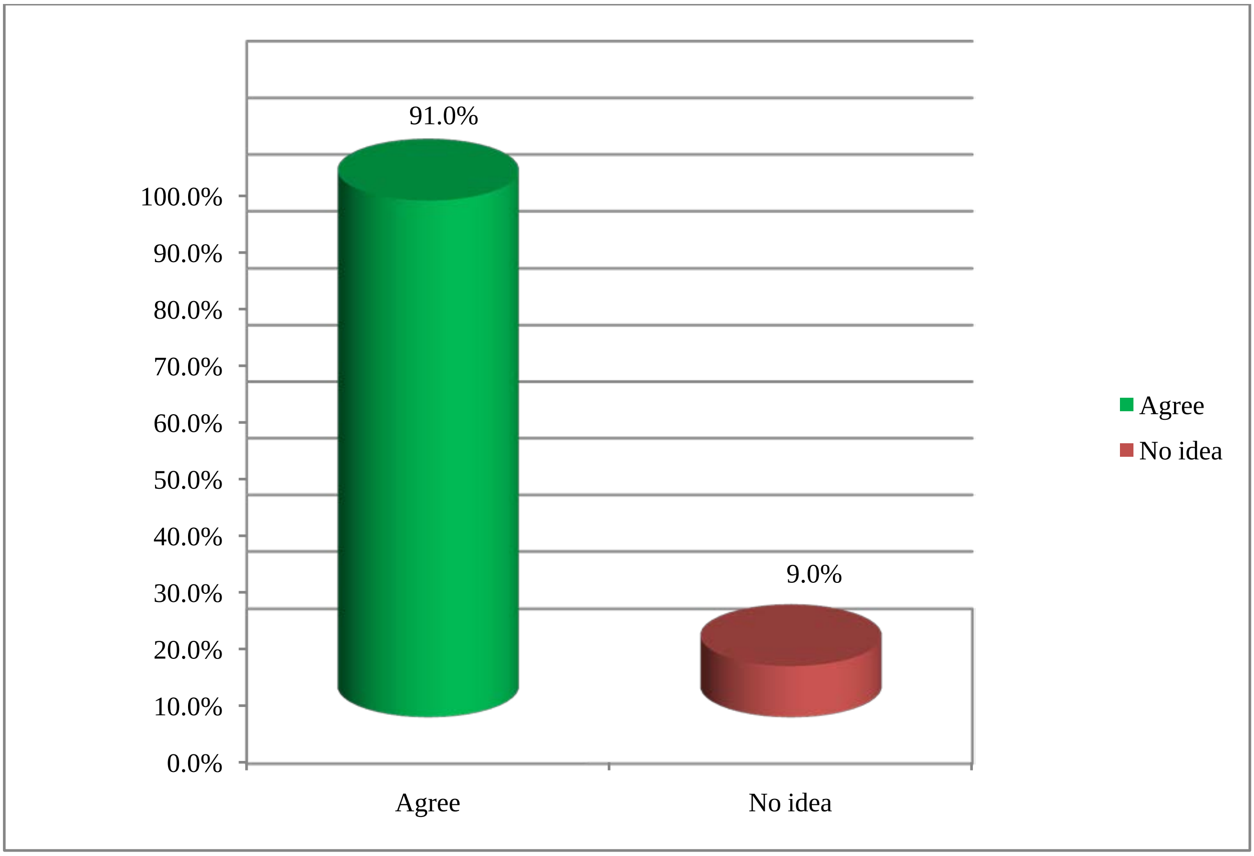

Figure 3.5: Whether Internal Control System can assist in improving the effectiveness of Corporate Governance

Table 3.5 and Figure 3.5 above indicated that 91.0% of the respondents agreed that ICSs could assist in improving the effectiveness of Corporate Governance while 9.0% of the respondents had no idea on whether ICSs could assist in improving the effectiveness of Corporate.

From the above analysis it can be understood that internal control systems assist in improving the effectiveness of corporate governance.

3.7 How Internal Control Systems contribute to effective corporate governance

The respondents' description on how internal control systems contribute to effective corporate governance were presented and analyzed as below:

Table 3.6: How Internal Control Systems contribute to effective corporate governance

How Internal Control Systems contribute to effective corporate governance	Frequency	Percentage (%)
Reduce costs due to theft, pilferages and obsolescence	61	78.2
Promote accountability and control on company resources	40	51.3
Prevent losses from occurring and enables timely detection of errors that have occurred	53	67.9
Provides assurance on the reliability of financial information generated through the company's financial statements	59	75.6
Provide assurance on continuity of the company processes in the absence of some key employees	27	34.6
Ensures accurate and timely management reports	47	60.3

Sources: Author's own research – Coastal Bottlers Limited

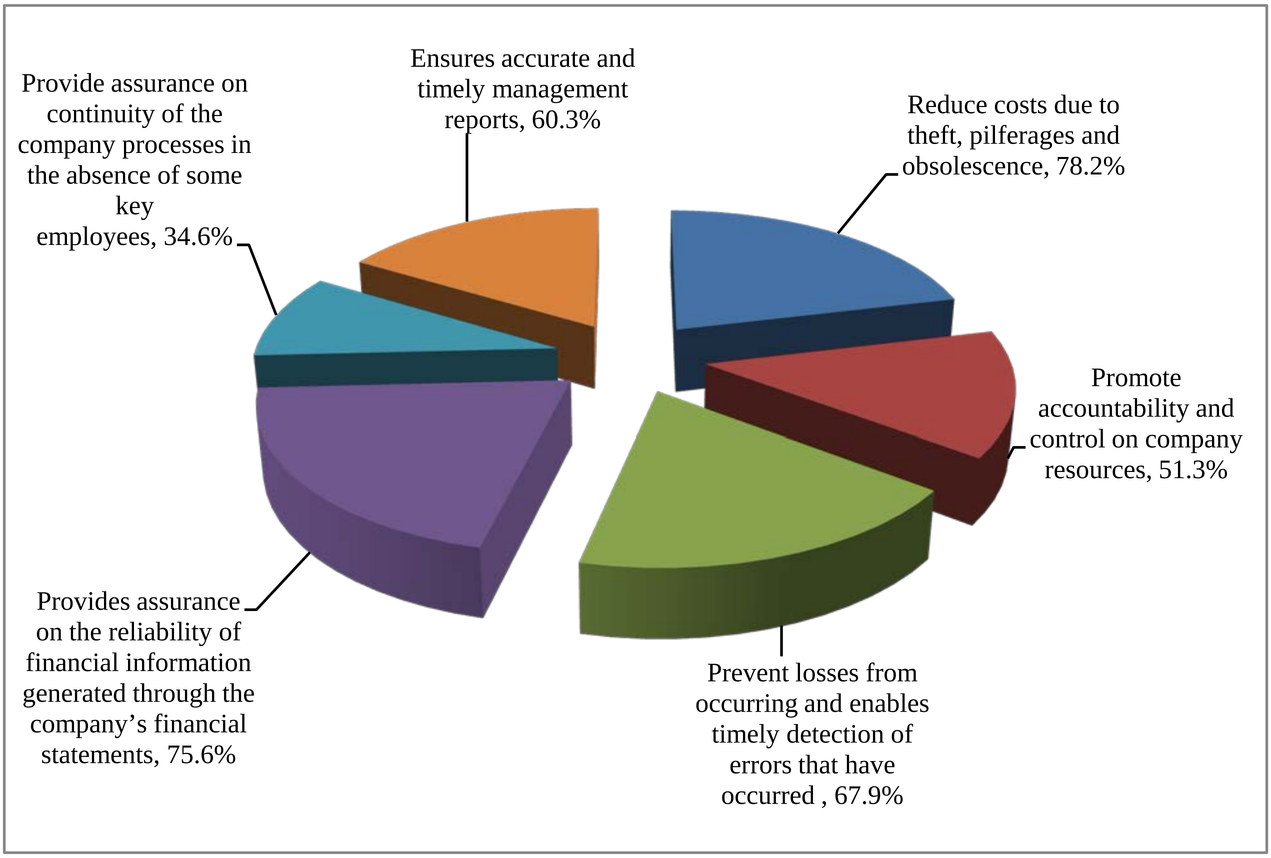

Figure 3.6: How Internal Control Systems contribute to effective corporate governance

Table 3.6 and Figure 3.6 above showed that 78.2% of the respondents described that internal control systems contribute to effective corporate governance through reducing costs caused by theft, pilferage and obsolescence; 51.3% of the respondents described that ICSs contribute through promoting accountability and control on company resources; 67.9% of the respondents described that ICSs through preventing losses from occurring and enables timely detection of errors that have occurred; 75.6% of the respondents indicated that ICSs contribute through providing assurance on the reliability of financial information generated through the company's financial statement; 34.6% of the respondents described that the ICSs contribute by providing assurance on continuity of the company processes in case of the absence of key employees while 60.3% of the respondents described that ICSs contribute to effective corporate governance by enabling accurate and timely management reports for efficient and effective operations.

The above analysis indicates that Internal Control Systems contribute to effective corporate governance by reducing costs caused by theft, pilferages and obsolescence; through providing assurance on the reliability of financial information generated through the company's financial statements; by preventing losses from occurring and enables timely detection of errors that have occurred; and ensures accurate and timely management reports.

3.8 Whether governance style affects the company's performance and state of affairs

The respondents' response on whether their managerial or governance style affects the company's performance and state of affairs of the company was presented and analyzed as below:

Table 3.7: Whether governance style affects the company's performance and state of Affairs

Whether governance style affects the company's performance and state of affairs	Frequency	Percentage (%)
Agree	69	88.5
No Idea	9	11.5
Total Respondents	78	100

Source: Author's own research – Coastal Bottlers Limited

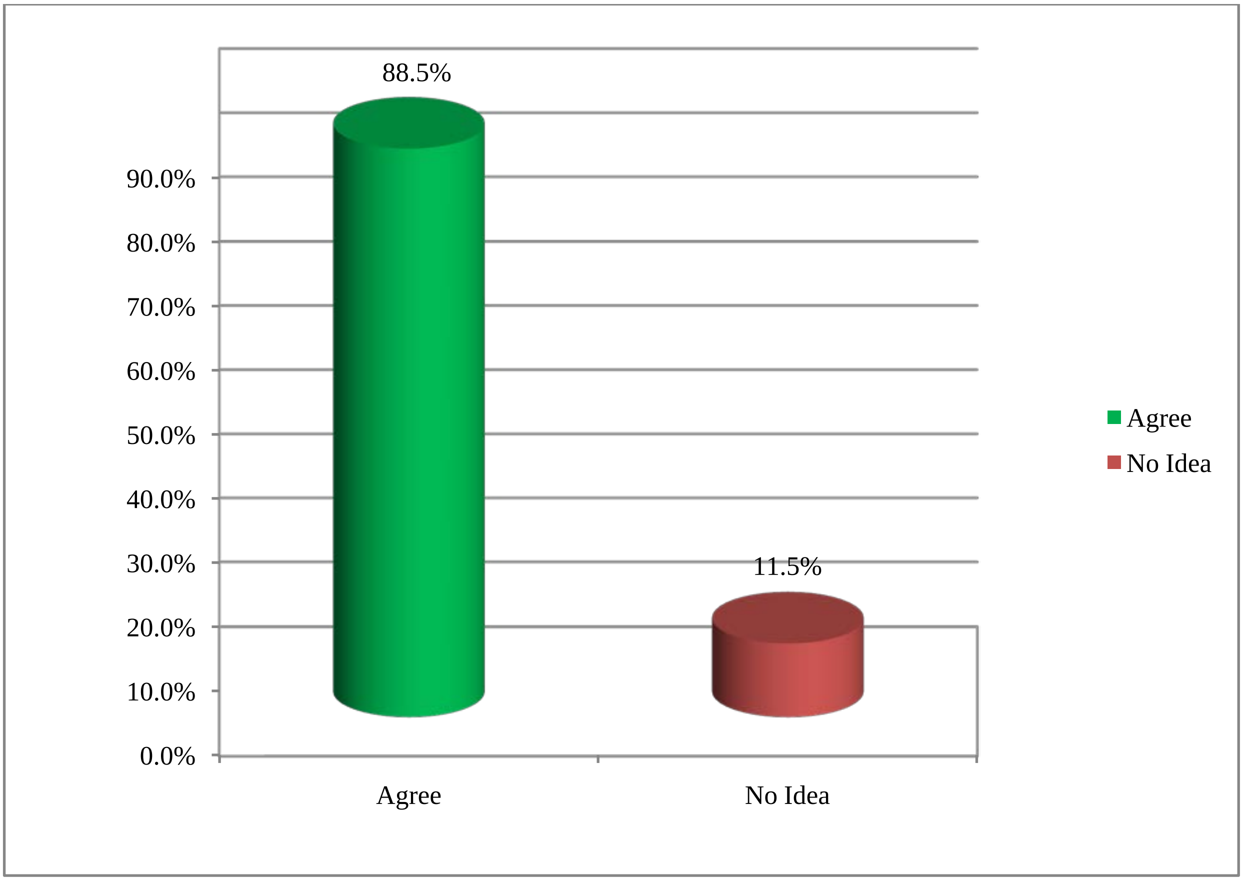

Figure 3.7: Whether governance style affects the company's performance and state of affairs

Table 3.7 and Figure 3.7 above indicated that 88.5% of the respondents agreed that the governance or managerial style adopted by the top management or board of directors affects the company's performance and state of affairs of the company while 11.5% of the respondents had no idea on whether governance style affects the company's performance and state of affairs of the company.

The above analysis indicates that the managerial or governance style adopted by the management and the board affects of affairs of the company.

3.9 How Financial Statements contribute to effective corporate governance

Table 3.8 and Figure 3.8 above indicated that 59.0% of the respondents described that financial statements contribute to effective corporate governance by highlighting controllable costs for managerial purpose; 52.6% of the respondents indicated that financial statements explain how the management has addressed risks associated with the company financial operations; 66.7% of the respondents described that financial statements reflect the management's operational efficiency by reflecting comparable result like current versus prior period; 89.7% of the respondents indicated that financial statements reflect company's financial position at any given time and performance over a specified period of time; 50.0% of the respondents indicated that financial statements reflect whether the company goals and objectives are being achieved or not while 80.8% of the respondents described that financial statements provide important managerial information for planning, monitoring performance and decision making purpose thus contributing to effective corporate governance in a company.

Responses collected from the respondents was presented in Table 3.8, and analyzed.

Table 3.8: How Financial statements contribute to effective corporate governance

How Financial statements contribute to effective corporate governance	Frequency	Percentage (%)
Financial statements highlight the controllable costs for management purpose	46	59.0
Financial statements reflect the company's financial position at any given time and performance over a specified period of time	70	89.7
Financial statements reflects whether the company goals and objectives are being achieved or not	39	50.0
Financial provide important managerial information for planning, monitoring performance and decision making purpose	63	80.8

Source: Author's own research – Coastal Bottlers Limited

The above analysis indicate that financial statements contribute to effective corporate governance through reflecting company's financial position at any given time and performance over a period of time; through provision of important managerial information for planning, monitoring performance and decision making purpose and reflecting the management's operational efficiency by reflecting comparable results like current versus prior period as described by majority of the respondents.

3.10 Analytical procedures in use in the company

The respondents' identified analytical procedures in use in the company were presented in Table 3.9, and analyzed.

Table 3.9: Analytical procedures in use in the company

Analytical procedures in use in the company	Frequency	Percentage (%)
Ratio analysis	69	88.5
Brand and pack analysis	53	67.9
Trend analysis	57	73.1
Ageing analysis	41	52.6
Regression analysis	38	48.7

Sources: Author's own research – Coastal Bottlers Limited

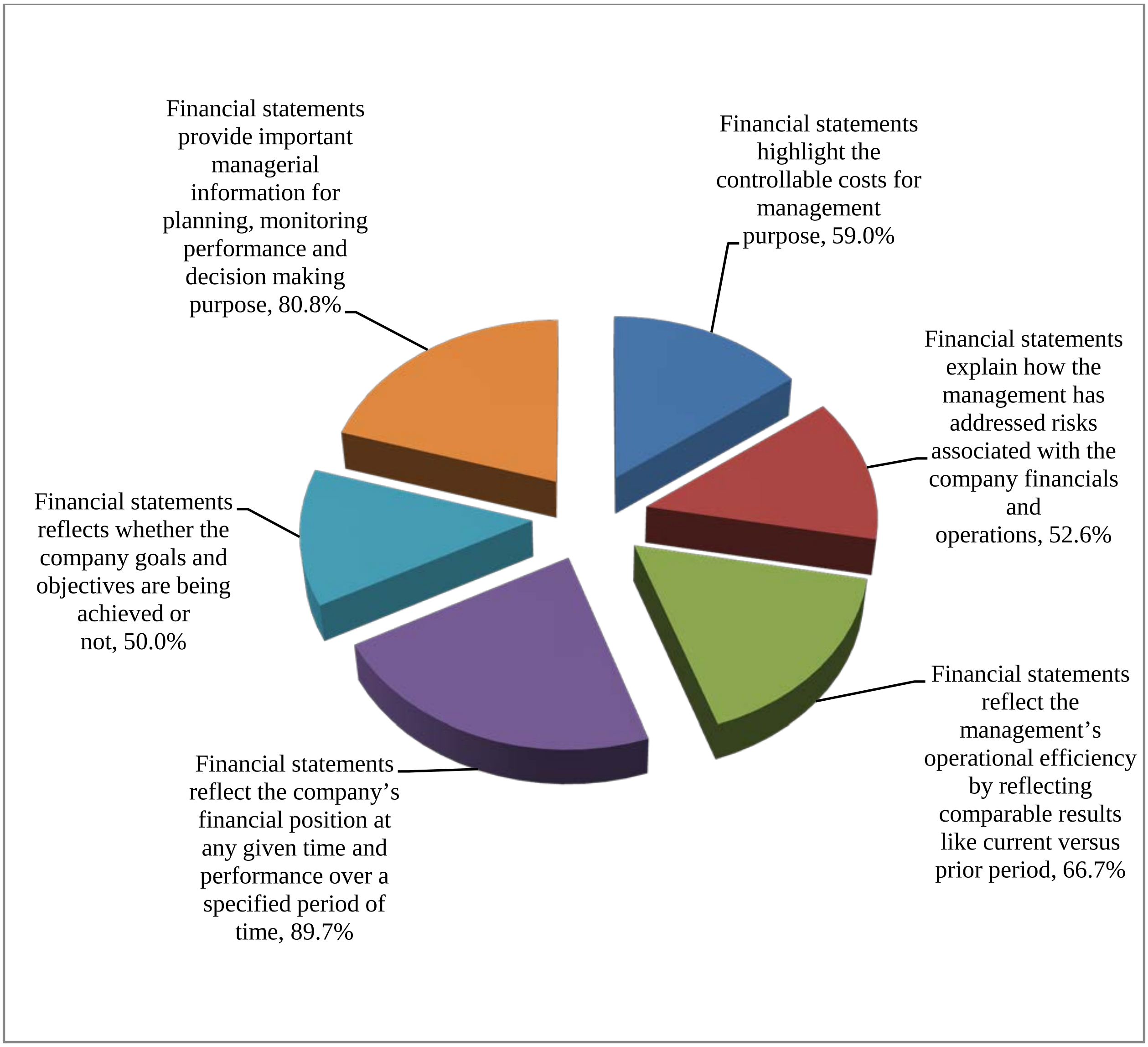

Figure 3.8: How Financial statements contribute to effective corporate governance

From the above Table 3.9 and Figure 3.9 indicates that 88.5% of the respondents described Ratio analysis as an analytical procedure that a company can use in its financial performance analysis; 67.9% of the respondents described Brand and pack analysis; 73.1% described Trend analysis; 52.6% described Ageing analysis while 48.7% described Regression analysis as an analytical procedure useful in financial analysis in the company.

The above indicate that Ratio analysis, Trend analysis, Brand and pack analysis and ageing analysis are analytical procedures which can be adopted by companies to help analyze their financial performance.

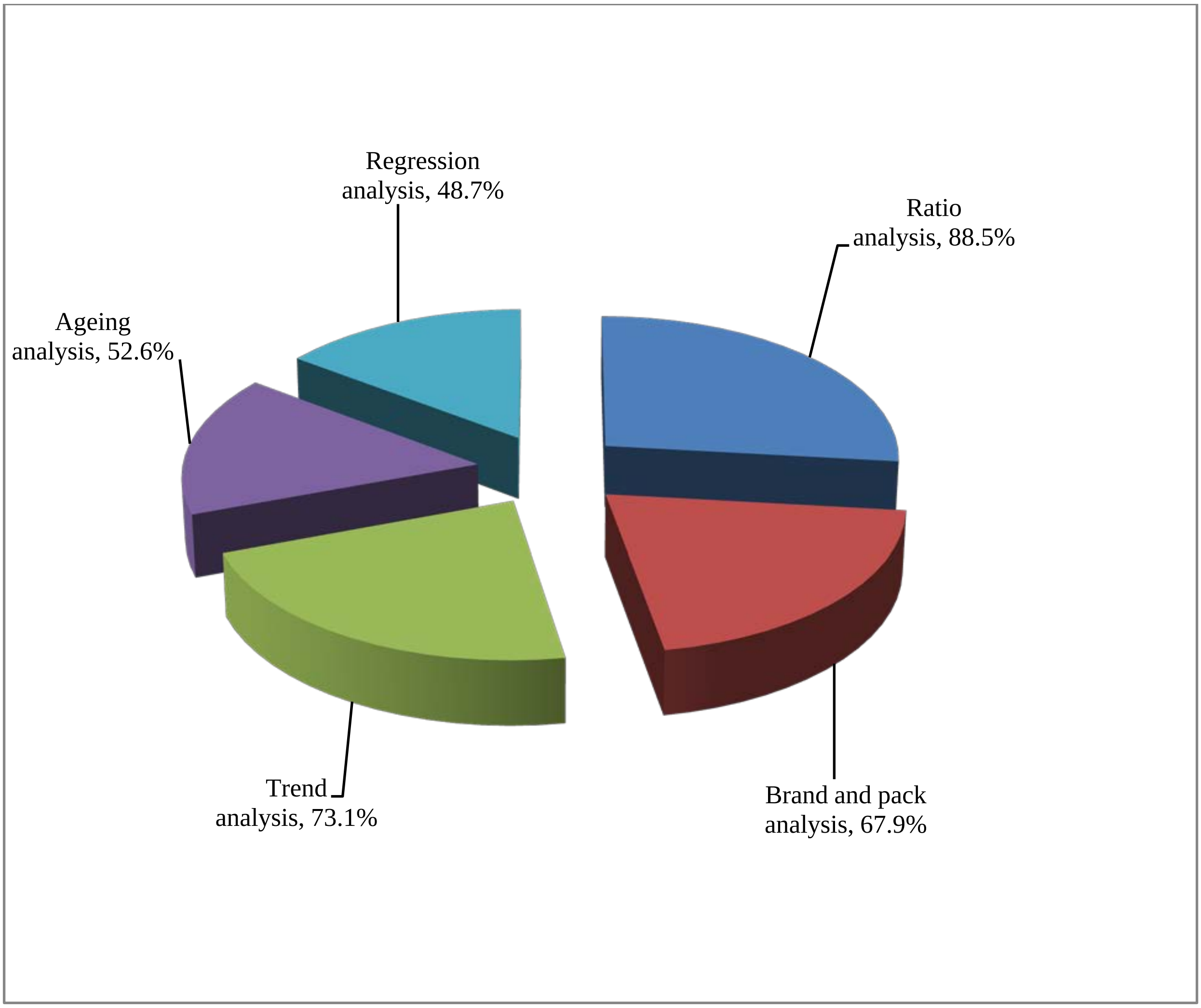

Figure 3.9: Analytical procedures in use in the company

3.11 Whether Analytical procedures help to improve corporate governance

The respondents' response on whether analytical procedures help to improve corporate governance were analysed below:

Table 3.10: Whether Analytical procedures help to improve corporate governance

Whether Analytical procedures help to improve corporate governance	Frequency	Percentage (%)
Agree	73	93.6
No Idea	5	6.4
Total Respondents	78	100

Sources: Author's own research – Coastal Bottlers Limited

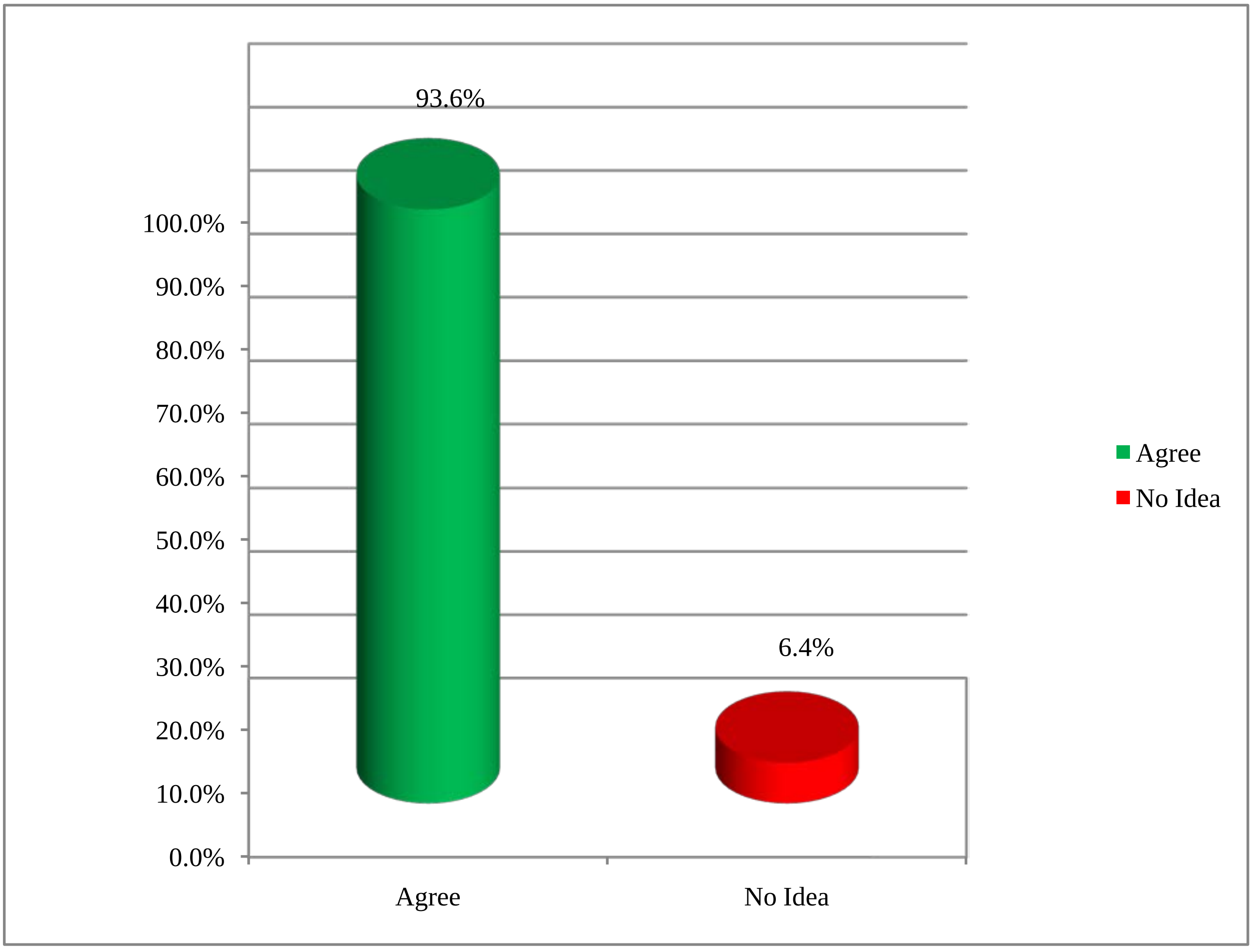

Figure 3.10: Whether Analytical procedures help to improve corporate governance

Table 3.10 and Figure 3.10 above reflected that 93.6% of the respondents agreed that analytical procedures help to improve corporate governance in companies while 6.4% had no idea on whether analytical procedures help to improve corporate governance.

The above analysis indicates that majority of the respondents agree that analytical procedures help to improve corporate governance.

3.12 How analytical procedures contribute to effective corporate governance

The respondents' responses on how analytical procedures contribute to effective corporate governance was presented Table 3.11, and analyzed.

From Table 3.11 and Figure 3.11 above, 64.1% of respondents described that analytical procedures contribute to effective corporate governance through providing top management with information to evaluate data and isolate the problem areas; 80.8% of the respondents stated the management to know whether the company is maximizing profit or not and try to find ways on how to improve the profitability of the company; 62.8% of the respondents stated that they help by ensuring minimization of waste through identification of adverse variance; 51.3% of the respondents described that they help management to identify risky areas of operations and performance while 53.8% of the respondents described that analytical procedures contribute to effective corporate governance by helping in human resource management by providing basis of employees' performance evaluation.

Table 3.11: How analytical procedures contribute to effective corporate governance

How analytical procedures contribute to effective corporate governance	Frequency	Percentage (%)
Providing top management with information to evaluate data and isolate the problem areas	50	64.1
They help the management know whether the company is maximizing profit or not which enables the management to find ways on how to improve the profitability of the company	63	80.8
Helps ensure minimization of waste through identification of adverse variance	49	62.8
Helps management to identify risky areas of operations and performance	40	51.3
They help in human resource management as employees are evaluated based on their performance reflected by the various activity ratios	42	53.8

Sources: Author's own research – Coastal Bottlers Limited

The above indicates that analytical procedures contribute to effective corporate governance by providing the management with information indicating whether the company is making a profit or not; providing the top management with information to evaluate data and isolate the problem area; and through identification of adverse variance thus helping management to minimize waste.

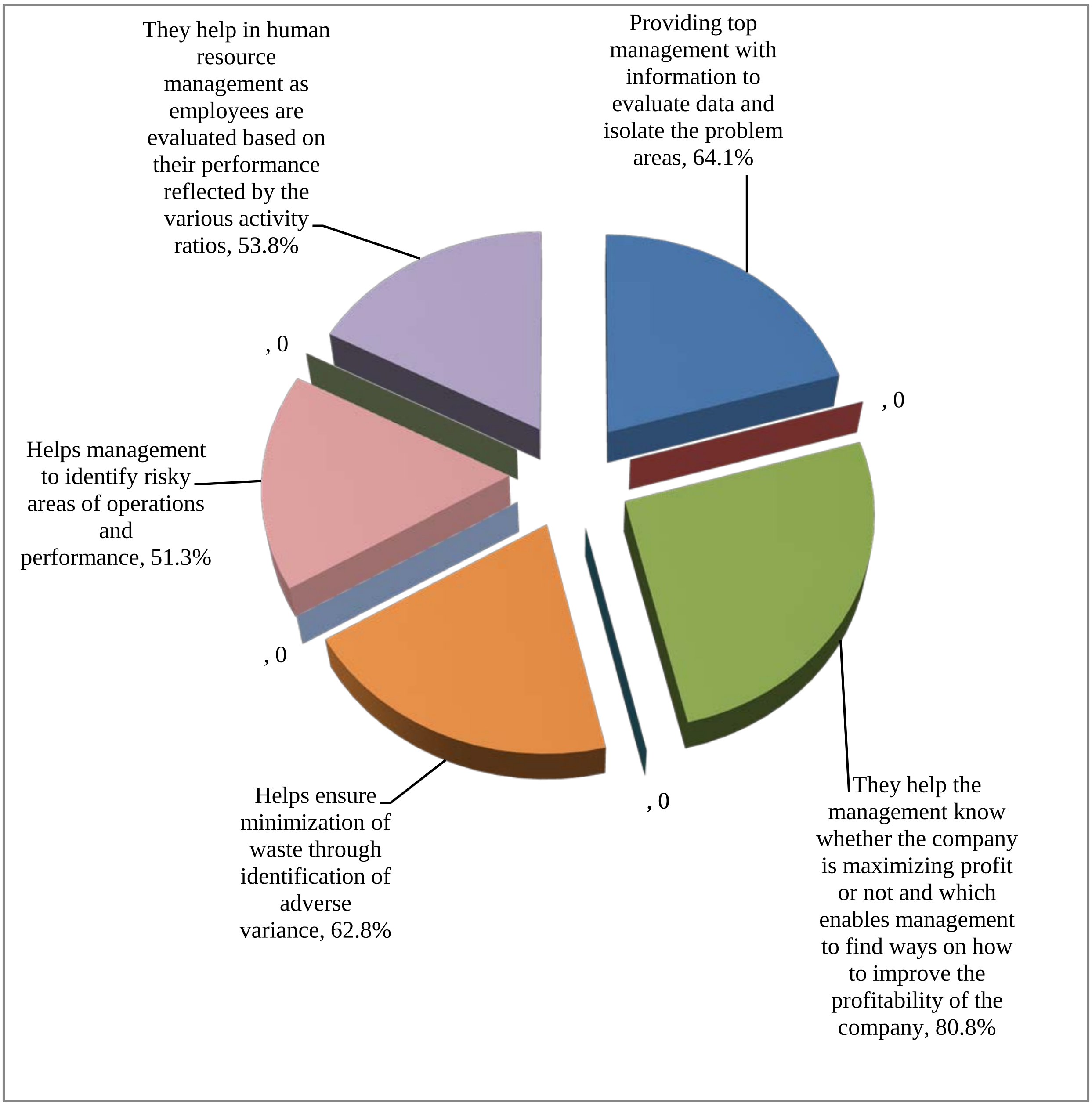

Figure 3.11: How analytical procedures contribute to effective corporate governance

14.13 Whether financial auditors are interested in operational results

The respondents' results on whether financial auditors are interested in operational results or not were analysed as below:

Table 4.12: Whether financial auditors are interested in operational results

Whether financial auditors are interested in operational results	Frequency	Percentage (%)
Agreed	28	49.1
No Idea	17	29.8
Disagreed	12	21.1
Total Respondents	57	100

Sources: Author's own research – Coastal Bottlers Limited

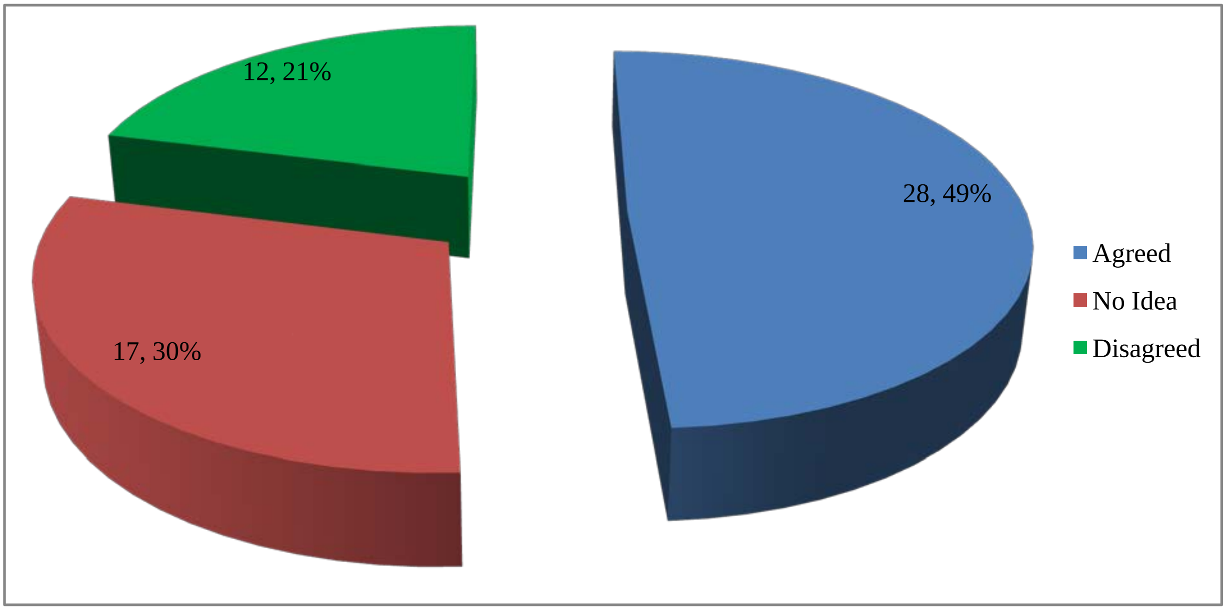

Figure 3.12: Whether financial auditors are interested in operational results

Table 3.12 and Figure 3.12 above, 49.1% of the respondents agreed that financial auditors were interested in operational results of the various departmental and section heads; 29.8% of the respondents had no idea as to whether or not financial auditors were interested in their operational results while 21.1% of the respondents disagreed on the fact that financial auditors are interested in their operational results.

From the above analysis, it can be noted that that financial auditors are interested in all the departments since all the departments' performance directly or indirectly contribute to the overall corporate performance.

3.14 How financial auditor's reports contribute to effective corporate governance

The results of the respondents on how financial auditor's reports contribute to effective corporate governance were analysed as below:

Table 3.13: How financial auditor's reports contribute to effective corporate governance

How financial auditor's reports contribute to effective corporate governance	Frequency	Percentage (%)
They encourage transparency and accountability by the management	53	67.9
They provide confidence to the stakeholders about the efficiency and effectiveness of the management's operational and control systems	61	78.2
They highlight areas where the internal control systems are weak and recommending on how to strengthen them	59	75.6
They enables the management to know whether they are compliant in all respects to laws and standards thus motivate them further to improve on their governance	65	83.3
The reports help the board and management to get improve on their performance as the shareholders would either retain them or fire them depending on the financial auditors report	42	53.8

Source: Author's own research – Coastal Bottlers Limited

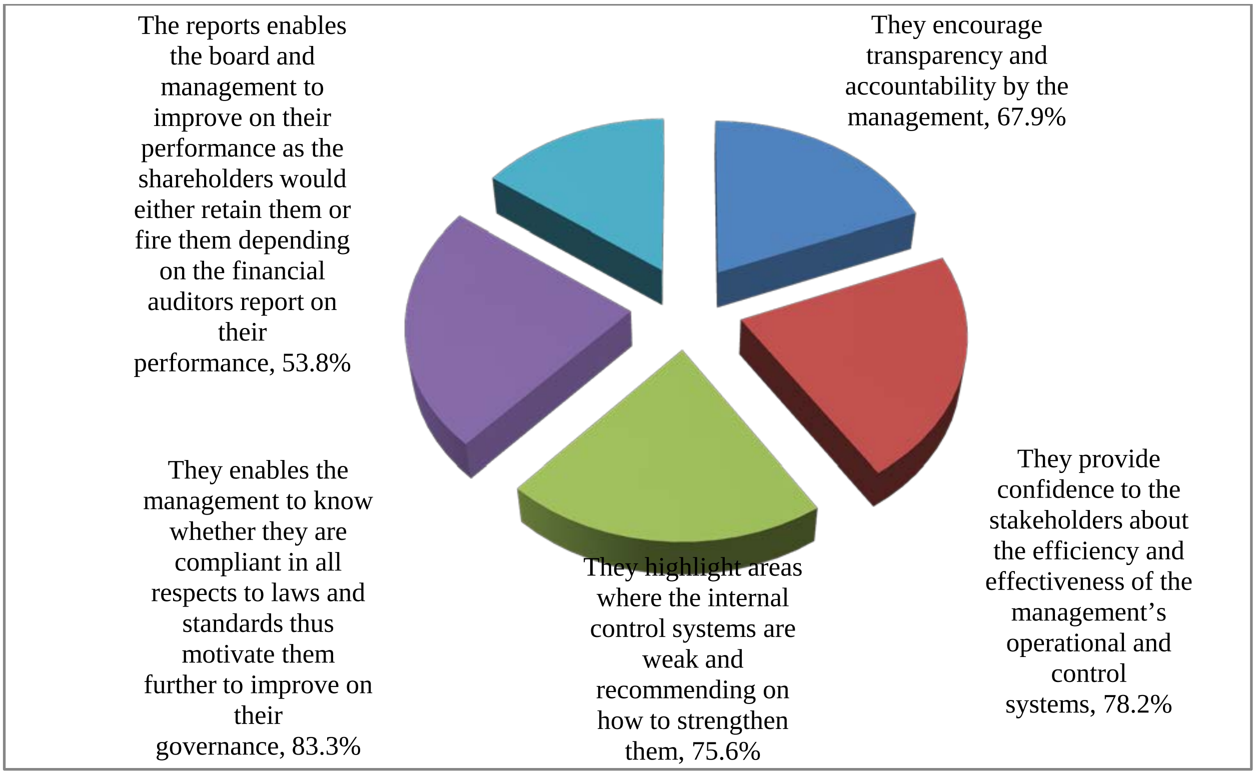

Figure 3.13: How financial auditor's reports contribute to effective corporate governance

Table 3.13 and Figure 3.13 above indicated that 67.9% of the respondents described that financial auditor's reports encourage transparency and accountability by the management which contributes to effective corporate governance; 78.2% of the respondents stated that financial auditor's contribute to effective corporate governance by providing confidence to the stakeholders about the efficiency and effectiveness of the management's operational and control systems; 75.6% of the respondents described that audit reports highlight areas where internal control systems are weak and recommending on how to strengthen them thus contributing to effective corporate governance; 83.3% of the respondents described that auditors reports enables the management to know whether they are compliant in all respects to laws and standards thus motivating them further to improve on their governance; while 53.8% of the respondents described financial auditor's reports as enabling the board and management to improve on their performance as the shareholders would either retain them or fire them depending on the financial auditor's reports on their performance.

The above analysis of the respondents' responses indicates that financial auditor's reports contribute to effective corporate governance by enabling the management to know whether they are compliant in all respects to laws and standards; by providing confidence to the stakeholders about the efficiency and effectiveness of the management's operational and control systems; by highlighting areas where internal control systems are weak and recommending on how to strengthen them; and by encouraging transparency and accountability by the management.

4. Conclusion

From the findings, we can derive the following conclusions:

Internal Control Systems such as segregation of duties, internal checks and balances, daily physical stock take and reconciliations contribute to effective corporate governance by reducing costs due to theft, pilferages and obsolescence; providing assurance on the reliability of financial information generated through the company's financial statements; and preventing losses from occurring and enabling timely detection of errors that occurred.

Financial statements affect the governance style adopted by the board and management and contribute to effective corporate governance by reflecting the company's financial position at any given time and performance over a specified period of time; by providing important managerial information for planning, monitoring performance and decision making; by reflecting the management's operational efficiency by reflecting comparable results like current versus prior period results; and by highlighting the controllable costs for management purpose.

Analytical procedures such as ratio analysis, trend analysis, Brand and pack analysis, and ageing analysis contribute to effective corporate governance by enabling the management to know whether the company is maximizing profit or not; providing the management with information to evaluate data and isolate the problematic areas; and by ensuring minimization of waste through identification of adverse variances.

Financial auditor's reports contribute to effective corporate governance by enabling the management to know whether they are compliant in all respect to laws and standards which motivates them to improve on their governance and performance; by providing confidence to the stakeholders about the efficiency and effectiveness of the management's operational and control systems; by highlighting areas where internal control systems are weak and provide recommendations on how to strengthen them; and by encouraging transparency and accountability by the management.

5. Acknowledgements

I offer many thanks to the management of Coastal Bottlers for accepting my request to carry out my research in their company.

I would like to thank my supervisor, Dr. Francis Kerongo who took his precious time to help me and offered me unyielding support and advise that steered my study throughout.

Finally, I would like to thank all lecturers for their excellent lectures upon which this project was based. In addition, I extend my profound gratitude to my classmates and all those who interacted with me during my time of study.

6. References

[1] AF. V. Staden (2011). *The Ultimate goal of all science is the search for truth. Research Design and Methodology*. [On-line]. pp.187-189. Available: http://upetd.up.ac.za/thesis/available/etd-10162011-152641/unrestricted/06chapter8.pdf. [Oct. 23, 2013].

[2] B. Okundi (2012). “FiRE award aims to promote sound financial reporting systems”. *The Accountant Journal of the Institute of Certified Public Accountants of Kenya,* December-January 2013, pp.26-27.

[3] C. R. Kothari (2004); “Research Methodology Methods and Techniques”. New Age International (P) Ltd, publishers.

[4] B. V. Elsevier& T. Jr. Limperg(1932). *The function of the accountant and the Theory of Inspired Confidence*.[On-line]. Available:http://www.limperginstituut.nl/assets%20limperg/Publicatie%20.The%20social%20responsibility%20of%20the%20auditor.pdf.Limperg Instituut, Inter-university institute for accountancy, Mensinge 2, 1083 HA Amsterdam, The Netherlands, [Nov. 20, 2013].

[5] D. Hartzler& C. Bright (2012). *Corporate governace. International Finance Corporation: World Bank Group*. [On-line]. Available: http://www.ifc.org/wps/wcm/connect/ topics_ext_content external corporate site/corporate+ governance/overview [Nov. 20, 2013].

[6] Financial Reporting Council (2003).*Accountability and Audit. The Combined Code on Corporate Governance*. [On-line] pp. 15-17. Available:http://www.frc.org.uk/combined.cfm [Nov. 21, 2013].

[7] G. Z. Jin (2005). “Competition and Disclosure Incentives: An Empirical Study of HMOs”. *The RAND Journal of Economics*. [On-line] Vol. 36, No. 1 (Spring, 2005), pp. 93-112. Available:http://www.jstor.org/stable/1593756 [Oct. 25, 2013].

[8] International Auditing and Assurance Standards Board (2012). ISA 200: “Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing”. Handbook of

International Quality Control, Auditing Review, Other Assurance, and Related Services Pronouncements (2012thed.) Volume I. International Federation of Accountants publishers.

[9] International Auditing and Assurance Standards Board (2012). ISA 250: Consideration of Laws and Regulations in an Audit of Financial Statements".Handbook of International Quality Control, Auditing Review, Other Assurance, and Related Services Pronouncements (2012thed.) Volume I. International Federation of Accountants publishers. International Federation of Accountants publishers.

[10] International Auditing and Assurance Standards Board (2012). ISA 260: "Communication with Those Charged with Governance". Handbook of International Quality Control, Auditing Review, Other Assurance, and Related Services Pronouncements (2012thed.) Volume I. International Federation of Accountants publishers.

[11] International Auditing and Assurance Standards Board (2012). ISA 315: "Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment".Handbook of International Quality Control, Auditing Review, Other Assurance, and Related Services Pronouncements (2012thed.) Volume I. International Federation of Accountants publishers.

[12] International Auditing and Assurance Standards Board (2012). ISA 450: "Evaluation of Misstatements Identified during the Audit". Handbook of International Quality Control, Auditing Review, Other Assurance, and Related Services Pronouncements (2012thed.) Volume I. International Federation of Accountants publishers.

[13] International Auditing and Assurance Standards Board (2012). ISA 520: "Analytical Procedures". Handbook of International Quality Control, Auditing Review, Other Assurance, and Related Services Pronouncements (2012thed.) Volume I. International Federation of Accountants publishers.

[14] International Auditing and Assurance Standards Board (2012). ISA 700: "The Auditor's Report on Financial Statements". Handbook of International Quality Control, Auditing Review, Other Assurance, and Related Services Pronouncements (2012thed.) Volume I. International Federation of Accountants publishers.

[15] J. K. Kihumba(2013). "Overview of Corporate Governance"**.** *The Journal of the Institute of Certified Public Accountants of Kenya. December-January 2013. pp*.40-41.

[16] J. P. H Fan & T. J. Wong (2001). *Do auditors perform a corporate governance role in emerging market? Evidence in Asia*. William Davidson Institute working paper 400. [On-Line]. Available:http://www.wdi.bus.umich.edu [Nov. 22, 2013].

[17] J. W. Murray (2013). *Going Concern*. [On-line]. Available:http://biztaxlaw.about.com/od/glossaryg/a/goingconcern.htm [Sept. 28, 2013].

[18] J. C. Anderson, K. K Moreno & J. M. Mueller (2003). *The Effect of Client vs. Decision Aid as a Source of Explanations upon Auditors' Sufficiency Judgments: A Research Note. Behavioral Research in Accounting*: February 2003, Vol. 15, No. 1, [On-line]. pp. 1-11. Available:http://dx.doi.org/10.2308/bria.2003.15.1.1 [Oct. 18, 2013].

[19] Libby Robert &M. Fredrick David (1990). Experience and the organisation of auditors' knowledge. *Managerial Auditing Journal*[On-line]. ISSN: 0268-6902. MCB UP Ltd. [Oct. 15, 2013].

[20] M. Sandelowski (2000). *Focus on Research Methods: Whatever happened to qualitative description?*[On-line].pp.337-338.Available:http://www.wou.edu/~mcgladm/Quantitative%20Methods/optional%20stuff/qualitativ

e%20descryption.pdf. [Oct. 17, 2013].

[21] N. Langberg& K. Sivaramakrishnan (2008). “Voluntary Disclosures and information production by analysts”. *Journal of Accounting and Economics*. [On-line]. Volume 46, Issue 1, September 2008, pp. 78–100. Available:http://www.sciencedirect.com/science/article/pii/S016541010700078X [Sept. 26, 2013].

[22] P. Sarbanes &M. G. (2002).“Sarbanes - Oxley Act”. [On-line].Pub.L. 107-204 [1], 116 Stat. 745, enacted July 30, 2002., pp. 3-9. Available:http://logitax.hu/SOX.pdf[Sept. 21, 2013].

[23] Pwc (2013). *Understanding a financial statement audit - pwc*. [On-line] pp. 2. Available: http://www.pwc.com/en_GX/gx/audit-services/publications/assets/pwc-understanding- financial-statement-audit.pdf. [Sept. 25, 2013].